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In the Supreme Court
OF THE
United States

OCTOBER TERM, 1957

No. 384

KAL W. LINES, *Petitioner,*

vs.

STATE OF CALIFORNIA, DEPARTMENT OF EMPLOYMENT, *Respondent.*

CONSENT TO FILING OF AMICUS CURIAE BRIEF
and
BRIEF OF THE CALIFORNIA STATE FEDERATION OF LABOR, A.F.L., AS AMICUS CURIAE, IN SUPPORT OF THE PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS, NINTH CIRCUIT.

CALIFORNIA STATE FEDERATION OF LABOR,
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STATE OF CALIFORNIA, DEPARTMENT OF EMPLOYMENT, *Respondent.*

CONSENT TO FILING OF AMICUS CURIAE BRIEF.

The undersigned are attorneys for the parties to the above-entitled action and hereby consent to the filing of an amicus curiae brief by Charles P. Scully on behalf of the California State Federation of Labor, A.F.L., and its affiliated members, who number in

excess of one and one-quarter million wage earners in the State of California.

Dated, San Francisco, California,
September 11, 1957.

KAL W. LINES,
Petitioner,
By MAX H. MARGOLIS,
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STATE OF CALIFORNIA, DEPARTMENT OF EMPLOYMENT,
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BRIEF OF THE CALIFORNIA STATE FEDERATION OF LABOR, A.F.L., AS AMICUS CURIAE, IN SUPPORT OF THE PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS, NINTH CIRCUIT.

PRELIMINARY STATEMENT.

Upon permission first being duly had and received, pursuant to stipulation of the parties in the above entitled matter, Charles P. Scully is submitting herewith this brief, *amicus curiae,* on behalf of the California State Federation of Labor, A.F.L., and its affiliated members, who number in excess of one and

one-quarter million wage earners in the State of California, pursuant to Rule 42 of the Revised Rules of the Supreme Court of the United States.

The interest of the California State Federation of Labor stems from the fact that the issues presented herein necessarily affect every one of its members, as well as all wage earners in the State of California.

The undersigned has read the petition for writ of certiorari and is familiar with the contents thereof and the matters stated herein are not cumulative.

OPINIONS BELOW.

The opinion of the Referee in Bankruptcy is unreported.

The opinion of the District Court, reversing the order of the Referee in Bankruptcy, is reported in 147 F. Supp. 93.

The opinion of the Court of Appeals in affirming the judgment of the District Court is reported in 242 F. (2d) 201.

The opinion of the Court of Appeals in denying the petition for rehearing is unreported.

STATUTES INVOLVED.

California Unemployment Insurance Code, Section 135 (Stats. 1953, c. 308, p. 1460, Sec. 135):

> "'Employing unit,' means any individual or type of organization, including any partnership,

association, trust, estate, joint stock company, insurance company, corporation whether domestic or foreign, and the receiver, trustee in bankruptcy, trustee or successor thereof, and the legal representative of a deceased person, which has, or subsequent to January 1, 1936, had, in its employ one or more individuals performing services for it within this State. All individuals performing services within this State for any employing unit which maintains two or more separate establishments within this State shall be deemed to be employed by a single employing unit for all the purposes of this division."

California Unemployment Insurance Code, Section 601 (Stats. 1953, c. 308, p. 1470, Sec. 601):

"'Employment,' means service, including service in interstate commerce, performed for wages or under any contract of hire, written or oral, express or implied."

California Unemployment Insurance Code, Section 926 (Stats. 1953, c. 308, p. 1480, Sec. 926):

"Except as otherwise provided in this article 'wages' means all remuneration payable for personal services, whether by private agreement or consent or by force of statute, including commissions and bonuses, and the reasonable cash value of all remuneration payable in any medium other than cash."

California Unemployment Insurance Code, Section 976 (Stats. 1953, c. 308, p. 1482, Sec. 976):

"Employer contributions to the Unemployment Fund shall accrue and become payable by every

employer for each calendar year with respect to wages paid for employment. The contributions are due and shall be paid to the department for the Unemployment Fund by each employer in accordance with this division and shall not be deducted in whole or in part from the wages of individuals in his employ."

California Unemployment Insurance Code, Section 987 (Stats. 1953, c. 308, p. 1485, Sec. 987):

"Each employer shall be liable for any and all contributions required to be made by his workers on account of wages which he has paid to them regardless of whether or not he has deducted the contributions from the workers' wages at the time they were paid, but no employer shall be liable for worker contributions required on behalf of himself or of any of his employees with respect to wages paid while there is in effect at the time the wages were paid a rule or regulation or interpretation of the director or of the department that such wages were not subject to such contributions."

California Unemployment Insurance Code, Section 2654 (Stats. 1953, c. 1371, p. 2946):

"For the purpose of this article wages due to any individual but unpaid within the time limit provided by law, shall be deemed wages paid to such individual."

California Labor Code, Section 201 (Stats. 1937, c. 90, p. 197, Sec. 201, as amended Stats. 1947, c. 769, p. 1849, Sec. 1):

"If an employer discharges an employee, the wages earned and unpaid at the time of discharge are due and payable immediately. An employer who lays off a group of employees by reason of the termination of seasonal employment in the curing, canning, or drying of any variety of perishable fruit, fish or vegetables, shall be deemed to have made immediate payment when the wages of said employees are paid within such reasonable time as may be necessary for computation and payment thereof; provided, however, that such reasonable time shall not exceed 72 hours, and further provided that payment shall be made by mail to any such employee who so requests and designates a mailing address therefor."

California Labor Code, Section 224 (Added Stats. 1937, c. 357, p. 774, as amended Stats. 1955, c. 496, Sec. 1):

"The provisions of Sections 221, 222 and 223 shall in no way make it unlawful for an employer to withhold or divert any portion of an employee's wages when the employer is required or empowered so to do by state or federal law or when a deduction is expressly authorized in writing by the employee to cover insurance premiums, hospital or medical dues, or other deductions not amounting to a rebate or deduction from the standard wage arrived at by collective bargaining or pursuant to wage agreement or statute, or when a deduction to cover health and welfare or pension plan contributions is expressly authorized by a collective bargaining or wage agreement."

Bankruptcy Act, Section 64(a)(1), (2), (4) (11 U.S.C., Section 104(a)(1), (2), (4)):

"(a) The debts to have priority, in advance of the payment of dividends to creditors, and to be paid in full out of bankrupt estates, and the order of payment, shall be (1) the actual and necessary costs and expenses of preserving the estate subsequent to filing the petition; the fees for the referees' salary fund and for the referees' expense fund; the filing fees paid by creditors in involuntary cases or by persons other than the bankrupts in voluntary cases; where property of the bankrupt, transferred or concealed by him either before or after the filing of the petition, shall have been recovered for the benefit of the estate of the bankrupt by the efforts and at the cost and expense of one or more creditors, the reasonable costs and expenses of such recovery; the costs and expenses of administration, including the trustee's expenses in opposing the bankrupt's discharge or in connection with the criminal prosecution of an offense punishable under chapter 9 of Title 18, or an offense concerning the business or property of the bankrupt punishable under other laws, Federal or State; the fees and mileage payable to witnesses as now or hereafter provided by the laws of the United States, and one reasonable attorney's fee, for the professional services actually rendered, irrespective of the number of attorneys employed, to the petitioning creditors in involuntary cases and to the Bankrupt in voluntary and involuntary cases, as the court may allow: *Provided, however,* that where an order is entered in a proceeding under any chapter of this title directing that bankruptcy be proceeded with, the costs and expenses incurred in the ensuing bankruptcy proceeding shall have priority in advance of payment of the unpaid

costs and expenses of administration, including the allowances provided for in such chapter, incurred in the superseded proceeding and in the suspended bankruptcy proceeding, if any; (2) wages not to exceed $600 to each claimant, which have been earned within three months before the date of the commencement of the proceeding, due to workmen, servants, clerks, or traveling or city salesmen on salary or commission basis, whole or part time, whether or not selling exclusively for the bankrupt; * * * (4) taxes legally due and owing by the bankrupt to the United States or any State or any subdivision; . . ."

QUESTION PRESENTED.

The sole issue presented for determination of this Court is whether a tax imposed upon an employer, based upon wages earned prior to the filing of the petition in bankruptcy, is properly allocated to the cost and expense of the administration of the bankrupt estate.

ARGUMENT.

I. UNDER THE PROVISIONS OF THE UNEMPLOYMENT INSURANCE CODE AND THE LABOR CODE OF CALIFORNIA, THE EMPLOYER CONTRIBUTION IN THIS CASE HAD ACCRUED PRIOR TO THE FILING OF THE PETITION IN BANKRUPTCY

The pertinent facts in this case are not in dispute and show that all of the wages upon which the employer contributions were based were earned prior to the filing of the petition in bankruptcy. The facts

further show that the trustee in bankruptcy did not continue the business of the bankrupt, did not employ any persons for wages, and did not pay or become liable for wages earned after the date of bankruptcy.

Section 976 of the California Unemployment Insurance Code provides that employer contributions are based upon wages paid to employees and that the transmittal of said contributions is deferred to a later date. Section 976 further establishes a prohibition against the deduction, in whole or in part, of the employer contribution from employee wages, thereby providing that said contribution is the sole responsibility of the employer.

Section 2654, of the California Unemployment Insurance Code, with respect to disability benefits, provides that "wages due to any individual but unpaid within the time limit provided by law, shall be deemed wages paid to such individual". "Employment" is defined by Section 601 of the California Unemployment Insurance Code as service performed for wages or under any contract of hire and Section 135 of the California Unemployment Insurance Code defines an "employing unit" as a person or organization which has in its employ one or more persons. Section 926, California Unemployment Insurance Code, defines "wages" as remuneration payable for personal services.

Therefore, considering the framework and definitions established by the above provisions, it becomes obvious that the trustee in bankruptcy was not an employing unit because he did not have in his employ

any persons who were to perform services for wages under any contract of hire and the nature of the employer contribution must be considered as a fixed and owing obligation as of the date of bankruptcy.

In this regard, the provisions of Section 201, California Labor Code, become crucial. That section provides that wages which are earned but unpaid at the time of the discharge of an employee, are deemed to be payable immediately. In this case the employees of the bankrupt were not retained after bankruptcy but were discharged and thus, their wages became due and payable immediately under the provisions of that section. The only logical conclusion that can be reached is that the corollary contribution of the employer, the payment of the employer contribution, also became due and payable at that time because the discharge of the employees precluded any further payment of wages to them and the amount of the contribution on their wages became calculable and fixed at that time.

Finally, it must be noted that the only deductions that are lawfully permitted by Section 224, California Labor Code, are those which are for the benefit of the *employee* and not the *employer*. 3 Ops. Atty. Gen. 178. Certainly, the allocation of the employer contribution to the first priority under Section 64(a)(1) of the Bankruptcy Act is a direct benefit to the employer for it allows the satisfaction of his sole obligation ahead of the payment of wages to the employee. It cannot be said that the employee might receive benefit through the payment to the Unemploy-

ment Fund of the employer contribution, for any such benefit would be at most indirect, whereas he would directly benefit from the full payment of wages due and owing to him.

As indicated by the above provisions of the California Labor and Unemployment Insurance Codes, the overriding state policy is to insure the full payment of wages which have been earned and that policy is not subordinated to the policy motivating the Unemployment Insurance legislation. In other words, the basic policy is to insure the payment of wages earned, rather than to insure contributions to the unemployment insurance fund which would detract from those wages. The policy of the Unemployment Insurance legislation is to assure and improve the economic status of wage earners but if *employer* tax obligations are allowed to be deducted from such wages, the economic position of working people must necessarily suffer.

Section 987, California Unemployment Insurance Code, gives clear support to the correctness of the above position. That section provides that the employer is liable for "any and all" employee contributions whether or not he has deducted them from the wages of the employees. This clearly means that even as to the employee contributions, the employer is personally liable, without further recourse against the employees. In effect, the allocation of the employer contribution to the first priority in bankruptcy, as to pre-bankruptcy wages, absolves the estate of the employer of his obligation for the employer contributions

when he is not allowed to do so even as to employee contributions under the provisions of the above section. Certainly, if an employer cannot release himself from his obligation for *employee* contributions, he and his successors should not be released from the *employer* contribution—his sole obligation.

II. THE EMPLOYER CONTRIBUTION—A TAX—CANNOT BE PROPERLY HELD TO BE AN EXPENSE OF ADMINISTRATION UNDER SECTION 64(a)(1) OF THE BANKRUPTCY ACT.

Under the Bankruptcy Act, the filing of a petition in bankruptcy is the date of cleavage and the assets are segregated for the benefit of creditors at that time. *United States v. Marxen,* 307 U.S. 200, 207, 208, 59 S.Ct. 811, 815. The holding of the Court below failed to examine the nature of the employer contribution with respect to the determination of whether or not, as of the date of cleavage, said obligation was fixed and owing.

As indicated above, under the California provisions, the California Department of Employment was a creditor of the bankrupt estate as of the date of the filing of the petition in bankruptcy. The reason for this contention is that all of the facts necessary for the computation of the assessment of the employer contribution were present as of that date, that is, all of the wages upon which such a contribution would be based were due and payable and no further wages were to be paid. The case of *United States v. New York,* 315 U.S. 510, 517, 62 S.Ct. 712, 715, held that an

obligation has *accrued* at such time when all the facts necessary for the computation or assessment of a tax are present. That case dealt with employer contributions to the Federal Unemployment Insurance Fund. In that case, too, the employer contribution was due and owing as of the date of bankruptcy but was not yet paid. The exact situation which exists in the instant case. That case compels a determination that the employer contribution in this case was a fixed and accrued obligation prior to bankruptcy.

It is also well settled that debts within any particular class of priority under Section 64(a) of the Bankruptcy Act, stand on an equal footing and must share on a pro rata basis without a priority within that particular class. *Missouri v. Erhart,* (C.C.A. 8, 1940) 111 F.(2d) 992, cert. den. 31 U.S. 67, 61 S.Ct. 43. Furthermore, Section 64(a)(1) provides that debts necessarily incurred in the *preservation* or the *administration* of the bankrupt estate are the only ones which can be included in first priority.

Certainly, it cannot be said that the employer contribution was in any way necessary to the preservation of the assets of the estate. Similarly, it cannot be said that the employer contribution was necessarily incurred in the administration of the estate, for, as indicated above, the trustee in bankruptcy did not continue the business and did not incur liability for wages earned after the filing of the petition in bankruptcy but took possession of the bankrupt estate for the sole purpose of liquidation. In the face of these facts, the only conclusion which can be reached is that the

employer contribution was not properly allocated to the first priority under the doctrine of *Missouri v. Erhart,* and amounted to a priority as against other obligations in the same class.

The Court below relied heavily upon the case of *United States v. Fogarty,* (C.A. 8th), 164 F.(2d) 26, in determining that employment and withholding taxes which were not payable at the time the petition in bankruptcy was filed were entitled to a classification and an expense of administration under Section 64(a). However, that Court did not recognize the basic distinction between this case and the *Fogarty* case, where the receiver, under chapter XI of the Bankruptcy Act, continued the business and continued to be liable for wages and taxes incurred after the filing of the arrangement petition. Therefore, the *Fogarty* case represents a situation where the trustee or receiver is the successor of the bankrupt as an *employer,* whereas in the instant case, the trustee is the successor of the bankrupt as a liquidator and not as an employer. In the former, tax obligations are incurred after bankruptcy but in the latter, tax obligations were incurred prior to bankruptcy.

The Court below further held that the employer's tax was not due or capable of ascertainment until the wages were paid. It has been indicated above that since the wages of the discharged employees became due and payable prior to the filing of the petition in bankruptcy, all of the factors necessary for the computation or calculation were present and existing at that time, as was the obligation of the employer.

The anomaly of the position taken by the Court below is that wages earned but not paid prior to the filing of the petition in bankruptcy are deemed sufficiently definite in amount to be allocated to the second priority under Section 64(a) but the employer tax which is irrevocably tied to those wages is not deemed sufficiently definite to be allocated to the fourth priority, so it therefore must be allocated to the first priority. Such a position is in complete disregard of the fact that the tax was not necessarily incurred in the preservation or the administration of the estate.

Even if it should be determined that the employer contribution had not accrued, under the provisions of the California Unemployment Insurance and Labor Codes, the conclusion that such a contribution would be entitled to the fourth and not the first priority under the Bankruptcy Act would be unchanged for the reason that State law cannot govern the priority allocation under that Act and the terms and provisions of Section 64(a)(1) would be controlling, with particular reference to the fact that the employer contribution was not necessary to the administration or preservation of the bankrupt estate. See *New Jersey v. Anderson*, 203 U.S. 483, 27 S.Ct. 137; *City of New York v. Feiring*, 313 U.S. 283, 285, 61 S.Ct. 1028, 1029. In that event, the test of *United States v. New York*, supra, would be controlling because all of the facts necessary for the computation or the assessment of the employer tax obligation were present and existing prior to or at the time of filing of the petition in bankruptcy.

CONCLUSION.

For each and every one and all of the above reasons, it is respectfully submitted that this Court should grant the petition for writ of certiorari to the United States Court of Appeals for the Ninth Circuit.

Dated, San Francisco, California,
September 11, 1957.

CALIFORNIA STATE FEDERATION OF LABOR,
By CHARLES P. SCULLY,
General Counsel.